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TESTIMONY OF TREASURER DEBORAH B. GOLDBERG

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Acknowledgments

Chairwoman Spilka, Chairman Dempsey and Members of the Committee – thank you for the opportunity to testify this afternoon on the Governor’s budget proposal and our state’s economic future.

Introduction and Economic Outlook

As treasurer, I often view my role as your chief financial officer. From managing daily cash flows and debt payments, to overseeing the state pension fund, to maximizing Lottery profits, we at Treasury are constantly evaluating how our financial decisions, working with you, impact the people we serve and the state we lead together.

Even as we now face what some have estimated to be a \$1.8 billion structural deficit, I remain cautiously optimistic about our economic prospects.

Because of a sound strategy for growth shaped by investments in our schools, our infrastructure and our people – we approach this upcoming year in far better economic shape than most other states.

But I also believe that the challenges we face today and the problems we anticipate demand robust public debate, not complacency. When I took this office nearly two months ago, I pledged to manage the state’s finances with the highest degree of fiscal responsibility. And I would not be fulfilling my commitment to the citizens I serve if I did not dive into the details and confront the tough questions looming before us for FY 2016.

Bond Rating

Due in large part to prudent fiscal management from this Committee, Massachusetts now has the highest bond rating in its history. While I am deeply proud of this accomplishment and the benefits it delivers to taxpayers, I remain keenly aware of the concerns that rating agencies share going forward.

First – our unfunded pension liability. I applaud you and the Administration for following through on last year’s commitment to aggressively fund our pension liability, increasing the state’s contribution in the pension fund line item by 10 percent for the next two years, and then 7 percent in the years that follow. We all understand that our continued attention to these obligations must remain one of our collective priorities.

However, I am concerned that while the Governor’s proposed Early Retirement Incentive Program may offer significant savings in the short-term – savings all dependent on how many workers are included in any expansion of the proposal, how many workers voluntarily retire and how many workers the state eventually hires back – it also may create new potential problems in the long-term.

The proposal increases our unfunded pension liability. Then it takes this new obligation, and it spreads the state’s repayment plan out, reportedly over the next 15 years. Further analysis that evaluates the proposal’s savings and incurred costs of any final legislation would help clarify these concerns.

Second – our rainy day fund. Rating agencies and investors alike consistently point to our reserves as a source of fiscal strength, and building those reserves will be essential as we strive to both maintain and improve our bond rating. I know you and the Governor share my commitment to boost the rainy day fund significantly over the next four years, and I look forward to working together in a dynamic partnership to turn our vision into reality.

In the FY 2015 deficit reduction legislation, I supported diverting capital gains tax revenues over \$1 billion from the rainy day fund given the extraordinary circumstances of few options on the table and little time to act. But I am worried that reliance on such a practice will raise red flags to the same rating agencies that have praised our mutual commitment to growing the rainy day fund.

I raise these concerns deeply cognizant of the exceedingly difficult task you face in balancing a budget where state spending continues to grow at a far quicker pace than revenue. As the Committee prepares to propose its own budget, diverting revenues from our reserves should only be a true last resort after we discuss a range of other feasible options.

Lottery and Local Aid

Lottery profits provide the number one source of unrestricted local aid to our 351 cities and towns. These dollars are critical to allowing our communities to adapt to

unanticipated costs, including, as we have learned this year, the all too unpredictable snow and ice budgets!

For more than 40 years, from revamped game mechanics and appearances, to innovative promotional products, to increased advertising, our strategic initiatives have positioned us to imagine the future and then seize it!

But new challenges and competition in the years ahead will test our ability to brand the Lottery and maximize returns.

Through March 7, total gross sales this year are at \$3.36 billion, up \$104.59 million or 3.21 percent over last year.¹

In January, I reported to you that we remained on track to meet our FY 2015 net profit projection of \$947.8 million. And I reported that with a level-funded \$8 million advertising budget, we anticipated returning \$925 million in FY 2016.² Yet midyear 9C cuts of nearly \$1.7 million in our administrative budget, advertising and monitor games have significantly reduced those estimates for both years.

Despite our best efforts to minimize the impact to revenue and profit and maintaining the lowest administrative costs out of any lottery in the country at just 2 percent of overall revenues, in February we lowered our net profit projection for FY 2015 by \$12.4 million to \$935.4 million.

We have also significantly lowered our FY 2016 net profit estimate by about \$27 million to \$897.8 million. Yet the cuts in the Governor's proposed budget, which differs greatly from our request to this Committee, would drive this number even lower, to an estimate of \$863.6 million.

Let me be very clear on this point. 9C cuts have already hurt Lottery profits, in effect hurting unrestricted local aid to our cities and towns. And the proposed cuts in H1 only cause Lottery profits to fall further.

While restored funding for FY 2016 will help raise this estimate, it will not entirely erase the impact of the cuts we have already suffered. The shelf life of games and ticket

¹ While overall FY 2015 sales are on the rise, a gradual shift in player purchases toward higher priced games that offer higher prize payouts has forced us to adjust our budgeted annual prize payout from 72.3 percent to 72.7 percent. Nearly 50 percent of all Instant Ticket sales in FY 2014 were derived from \$10, \$20 and \$30 games. To date in FY 2015, this percentage has increased to 53.7 percent. This shift has mitigated the positive impact of increased sales to the bottom line.

² In FY 2016 we will see an additional \$20 million impact to the Lottery's prize payout that will be awarded this fall – the result of a second chance prize from a 2009 Instant Ticket game. This prize is the official close of an Instant Ticket Mega Cash game that was released in October 2009 and officially sold out in August 2014. The Lottery eliminated the practice of offering Instant Tickets such as this with large end of game second chance prizes that are designed to be awarded one year after game sales have ended.

printing does not coincide neatly with the start and end of our fiscal year calendar. For the same reasons, cuts to our FY 2016 budget will also significantly impact FY 2017 revenue and profit estimates.

In our FY 2016 budget proposal to this Committee, we outlined two significant line-item increases, which are detailed further in your packets.

For the Lottery Administration line item (0640-0000) we are requesting \$88.98 million, or what amounts to a roughly \$6.15 million increase from the FY 2015 budget prior to 9C cuts. This amount consists almost entirely of mandatory expenditures, including \$1.15 million in CBA contract obligation and more than \$3.55 million in one-time costs to upgrade our communications technology. For example, our providers are no longer offering the land line cable communication system that we've depended on for decades. It is obsolete. And so we must complete the transition to a wireless system before December 2015, which carries with it significant start-up costs. This is critical to ensure our retailers can continue to place bets with no loss of revenue.³

For the Monitor Games line item (0640-0005), we are requesting \$3.18 million, which is level funding compared to the FY 2015 budget prior to 9C cuts.

For the Health and Welfare line item (0640-0096), we are requesting \$439,531, or what amounts to a \$66,586 increase from the FY 2015 budget prior to 9C cuts. This request is necessary to properly fund the formula in the Lottery's SEIU union contract.⁴

For the Advertising line item (0640-0010), we are requesting \$10 million, or what amounts to a \$2 million increase from the FY 2015 budget prior to 9C cuts.

The Lottery must operate in a rapidly evolving marketplace and will soon face competition from a slots parlor and casinos fighting for disposable income dollars. The Plainridge slots facility is slated to open this summer, and two licensed casinos will be operating in the state within the next few years. To address these challenges in FY 2016 and beyond, the Lottery must continue to develop solutions to retain and attract new players and remain relevant in an increasingly crowded marketplace. It is imperative that we continue to innovate and lead with proactive, not reactive strategies!

³ The technology enables our 7,500 retailers to confirm and place secure wagers from their store locations. The upgrade and migration from the existing frame relay cable system to a wireless solution must be completed by the end of December 2015. This increase covers the estimated cost of retiring the existing system and migrating over to a more advanced network. It is necessary that the Lottery run parallel systems for periods during this migration, to ensure that our retailers can continue to place bets with no loss of revenue. The additional funds requested reflect just more than \$1 million in inflation to the costs of carrying out our core revenue-generating business, including Instant Ticket printing, bet slip printing and postage or shipping, as well as \$350,000 in software renewals and upgrades, and minimal increases to a existing operational service contracts.

⁴ Prior to the new contract, which went into effect in July 2014, the cost was \$18.25 per full time employee per week. Under this contract, the cost inflated by \$3.25 per week per full time employee or a total of \$21.50, which amounts to an increase of \$66,586.

Over the years, we have proven that sales directly benefit from increased consumer awareness generated through integrated advertising campaigns.

A \$3 million increase in the Lottery's advertising budget from \$5 million in FY 2014 to \$8 million in FY 2015 enhanced our marketing, enabling us to reach markets outside of Boston and connect with new audiences through digital and mobile advertising.

Yet even at \$8 million, Massachusetts ranks last in the nation in advertising dollars as a percentage of sales.

States that generate a comparable level of sales, including Florida, California and New York, for example, have respective advertising budgets of \$37.5 million, \$65 million and \$92.2 million.

Increased advertising dollars have produced a return on investment of better than two to one! In fact, this year's holiday advertising campaign was even more successful, generating \$5 in profit for every \$1 spent on advertising.

As a businesswoman, I firmly believe that the last thing you do when you're trying to increase revenue is cut advertising. And especially not when new competition is moving into your backyard!

With a budget of \$10 million the Lottery would continue to innovate with cost-effective, efficient promotions and maximize our opportunity for increased revenue and profit return.

With an advertising budget of \$10 million, our net profit projection for FY 2016 will increase by about \$4 million to about \$901.5 million.

Economic Empowerment

As many of you are aware, four years ago the Legislature and the Treasurer's office established a Financial Literacy Trust Fund to provide access to financial education to residents across the Commonwealth. Yet as successful as our limited programs have been, they are not reaching enough citizens in enough communities.

That is why on day one, I launched a new Office of Economic Empowerment, led by a deputy treasurer with the deliberate goal of vastly expanding the capacity of this fund to incorporate a range of initiatives, including financial literacy, college savings plans and programming to support wage equality. I believe that when you invest in people, you empower people to invest in themselves. And that is precisely what we are trying to do with our new office. The more people are able to help themselves, the less they have to rely on a government sponsored safety net.

We are building a robust agenda with the goal of funding and expanding the Trust to leverage private sector and philanthropic money. But to do so, we need greater resources in the near term future.

Increased funding will help us hire a grant writer that will allow the Office to supplement its FY 2016 appropriation with a more robust fundraising strategy.

Today, I am respectfully requesting about \$897,000 for the Financial Literacy line item (0610-0010).

We are also requesting \$100,000 for the Commonwealth Covenant Fund line item (0610-3382), which provides tuition and loan-repayment scholarships for college graduates in STEM-related fields.

Madam Chairwoman and Mr. Chairman, I hope that in viewing this request you will keep in mind my intent to leverage the funding and form new public-private partnerships in pursuit of our shared goal of advancing and creating economic opportunity for the people of Massachusetts. I view the Financial Literacy Trust Fund as our vehicle to accomplish this goal.

ABCC

Today, in the interests of enhancing public safety across the Commonwealth, we are also requesting an increase in the Alcoholic Beverages Control Commission's (ABCC) Administration line item (0610-0050) from \$2.31 million in the FY 2015 budget prior to 9C cuts to \$3.15 million for FY 2016 to hire five additional investigators and other essential staff.

Year-after-year, the ABCC collects revenue nearly double its budgetary appropriation, this year generating more than \$4.2 million with only a \$2.3 million administrative budget.

In recent years we have seen an increase in transactions and license types, creating the need for additional resources at the agency. In the past four years the ABCC has seen an 8 percent increase in the number of retail and industry level licenses, in addition to a 21 percent increase in the number of license transactions processed. Moreover, the current licensing trend shows a dramatic increase in applications as a result of statutory changes, including the Direct Wine Shipper License, of which we have issued 498 year-to-date, the Caterer's License and the Farmer Pouring Permits, as well as numerous Excess Quota Licenses.

Investigative staffing has fallen from 40 positions in the 1980s to the current 15 positions, resulting in Massachusetts having the fifth lowest ratio of enforcement agents to licensees in the country.

Despite this staffing challenge, the ABCC has used innovative and effective enforcement programs to address alcohol-related problems in communities across the state.

If granted the funding to hire five new investigators, it will allow for broader coverage of alcohol law enforcement programs to prevent underage drinking and impaired driving, more efficient completion of license applications for businesses and smooth implementation of the Gaming Commission's Liquor Enforcement Unit rotational assignments without reducing core public safety-based programs.

We will continue our efforts to streamline operations and provide both efficient and effective management of the agency. But it is critical that we receive more resources to ensure we are doing all we can to prevent alcohol related injuries and incidents across the state.

Conclusion

In conclusion, I respectfully request that you fund Treasury, the Lottery, and the ABCC at the levels we submitted to the Joint Ways and Means Committee.

Thank you for the opportunity to testify. Once again, I applaud this Committee for the thoughtfulness and diligence with which you have tackled our budgetary challenges thus far. As we embark on the beginning of new public debate and dialogue for FY 2016, I look forward to being both your partner and resource in that discussion.

My colleagues and I will be happy to answer any questions you may have.